



OFFICIAL STUDY GUIDE 2001 EDITION



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COLLEGE-LEVEL EXAMINATION PROGRAM

Principles of Accounting

Description of the Examination

The Subject Examination in Principles of Accounting covers the information and skills taught in two semesters (or the equivalent) of college-level accounting. The emphasis of the exam is on financial and managerial accounting. Colleges may award credit for a one- or two-semester course in financial accounting including some managerial accounting topics, or for one semester of financial accounting and one semester of managerial accounting.

Battery-operated, hand-held calculators may be used during the exam, but all calculator memories must be cleared of both programs and data, and no peripheral devices such as magnetic cards or tapes are permitted. Although the exam was designed to be taken without a calculator, candidates may find one helpful for some of the questions.

The exam is 90 minutes long and includes approximately 78 multiple-choice questions to be answered in two separately timed 45-minute sections.

Knowledge and Skills Required

Questions on the exam require candidates to demonstrate one or more of the following abilities.

- Familiarity with accounting concepts and terminology
- Preparation, use, and analysis of accounting data and financial reports issued for both internal and external purposes
- Application of accounting techniques to simple problem situations involving computations
- Understanding of the rationale for generally accepted accounting principles and procedures

The subject matter of the Principles of Accounting exam is drawn from the following topics.

➤	<i>Approximate Percent of Examination</i>
60-70%	<p>Financial accounting (concerned with providing financial statements and reports of interest to company managers as well as bankers, investors, and other outsiders who must make a financial assessment of a company)</p> <ul style="list-style-type: none"> Generally accepted accounting principles Rules of double-entry accounting The accounting cycle Presentation of and relationships between general-purpose financial statements Valuation of accounts and notes receivable Valuation of inventories Initial costs of plant assets Depreciation Liabilities Investments Capital Cash and stock dividends Treasury stock Purchase and sale of merchandise Revenue and cost apportionments Cash control Division of profits and losses in partnership accounting Cash flow analysis
30-40%	<p>Managerial accounting (concerned with the use of accounting data for internal purposes to help management in planning and controlling functions of the company)</p> <ul style="list-style-type: none"> The manufacturing environment Analysis of departmental operations Process and job-order cost systems

➡ *Approximate Percent of Examination*

Standard costs and variances
Direct costing and absorption costing
Cost-volume profit (break-even) analysis
Use of differential (relevant) cost
Budgeting
Performance evaluation
Financial statement analysis

Sample Questions

The following 25 questions are similar to questions on the Principles of Accounting exam, but they do not appear on the actual exam. CLEP exams are designed so that average students completing a course in the subject can usually answer about half the questions correctly.

Before attempting to answer the sample questions, read all the information about the Principles of Accounting exam on the preceding pages. Additional suggestions for preparing for CLEP exams are provided in Chapter 1.

Try to answer correctly as many questions as possible. Then compare your answers with the correct answers given at the end of this examination guide.

Directions: Each of the questions or incomplete statements below is followed by five suggested answers or completions. Select the one that is best in each case.

1. The owner's equity in a business may derive from which of the following sources?
 - I. Excess of revenue over expenses
 - II. Investments by the owner
 - III. Accounts payable

(A) I only
(B) II only
(C) III only
(D) I and II only
(E) I, II, and III

(A) (B) (C) (D) (E)

2. Entries made on the books at the end of a period to take care of changes occurring in accounts are called
- (A) fiscal entries
 - (B) closing entries
 - (C) reversing entries
 - (D) correcting entries
 - (E) adjusting entries
- (A) (B) (C) (D) (E)
3. In accounting, net income should be defined as an increase in
- (A) assets
 - (B) cash
 - (C) merchandise
 - (D) sales
 - (E) capital
- (A) (B) (C) (D) (E)
4. Treasury stock may be correctly defined as
- (A) a corporation's own stock that has been issued and then reacquired
 - (B) new issues of a corporation's stock before they are sold on the open market
 - (C) stock issued by the United States Office of the Treasury
 - (D) any stock that a corporation acquires and holds for more than 90 days
 - (E) any stock held by a corporation that receives dividends in excess of 5% of initial cost of the stock
- (A) (B) (C) (D) (E)
5. The Accumulated Depreciation account should be shown in the financial statements as
- (A) an operating expense
 - (B) an extraordinary loss
 - (C) a liability
 - (D) stockholders' equity
 - (E) a contra (deduction) to an asset account
- (A) (B) (C) (D) (E)

6. If fixed expenses are \$26,000 and variable expenses are 75 percent of sales, the net income that would result from \$500,000 in sales is
- (A) \$ 75,000
(B) \$ 99,000
(C) \$200,000
(D) \$375,000
(E) \$401,000
- (A) (B) (C) (D) (E)
7. Cost of goods sold is determined by which of the following?
- (A) Beginning inventory plus net purchases minus ending inventory
(B) Beginning inventory plus purchases plus purchase returns minus ending inventory
(C) Beginning inventory minus net purchases plus ending inventory
(D) Purchases minus transportation-in plus beginning inventory minus ending inventory
(E) Net sales minus ending inventory
- (A) (B) (C) (D) (E)
8. Company X produces chairs of a single type; it has a plant capacity of 50,000 chairs per year and total fixed expenses of \$100,000 per year. Variable costs per chair are \$2 and the current selling price is \$5 per chair. At the beginning of 19x1, the company purchases a specialized machine that costs \$10,000, lasts one year, and reduces variable costs to \$1.50 per chair. If the company produces and sells at 90 percent of capacity, what is the net income for 19x1?
- (A) \$ 8,750
(B) \$23,000
(C) \$47,500
(D) \$50,000
(E) \$83,000
- (A) (B) (C) (D) (E)
9. The accounting concept that emphasizes the existence of a business firm separate and apart from its owners is ordinarily termed the
- (A) business separation concept
(B) consistency concept
(C) going-concern concept
(D) business materiality concept
(E) business entity concept
- (A) (B) (C) (D) (E)

10. Green Corporation with assets of \$5,000,000 and liabilities of \$2,000,000 has 6,000 shares of capital stock outstanding (par value \$300). What is the book value per share?

(A) \$200
 (B) \$300
 (C) \$500
 (D) \$833
 (E) None of the above

(A) (B) (C) (D) (E)

11. All the following T-accounts contain the correct sides that would be used for increasing and decreasing an account EXCEPT

(A) $\frac{\text{Revenue}}{\text{Decrease} | \text{Increase}}$ (B) $\frac{\text{Assets}}{\text{Increase} | \text{Decrease}}$

(C) $\frac{\text{Expenses}}{\text{Increase} | \text{Decrease}}$ (D) $\frac{\text{Owner's Equity}}{\text{Increase} | \text{Decrease}}$

(E) $\frac{\text{Liabilities}}{\text{Decrease} | \text{Increase}}$

(A) (B) (C) (D) (E)

12. At the end of the fiscal year, a company estimates that \$4,300 of Accounts Receivable will be uncollectible. If, prior to adjustment, the company's Allowance for Bad Debts account has a credit balance of \$1,600, what is the appropriate adjusting entry?

<u>DEBIT</u>	<u>CREDIT</u>	<u>AMOUNT</u>
(A) Allowance for Bad Debts	Bad Debts Expense	\$4,300
(B) Allowance for Bad Debts	Accounts Receivable	\$4,300
(C) Accounts Receivable	Allowance for Bad Debts	\$1,600
(D) Bad Debts Expense	Allowance for Bad Debts	\$2,700
(E) Bad Debts Expense	Accounts Receivable	\$2,700

(A) (B) (C) (D) (E)

13. A fast-moving widget stamping machine was purchased for cash. The list price was \$4,000 with an applicable trade discount of 20 percent and a cash discount allowable of 2/10, n/30. Payment was made within the discount period. Freight costs of \$100, F.O.B. origin, were paid. In order to install the machine properly, a platform was built and wiring installed for a total cost of \$200. The trial run costs were \$300 for labor and \$50 for materials. The cost of the machine would be recorded as

(A) \$3,626
(B) \$3,628
(C) \$3,786
(D) \$3,828
(E) \$4,178

(A) (B) (C) (D) (E)

14. All of the following expenditures should be charged to an asset account rather than to an expense account of the current period EXCEPT the cost of

(A) overhauling a delivery truck, which extends its useful life by two years
(B) purchasing a new component for a machine, which serves to increase the productive capacity of the machine
(C) constructing a parking lot for a leased building
(D) installing a new equipment item
(E) replacing worn-out tires on a delivery truck

(A) (B) (C) (D) (E)

15. In a period of rising prices, which of the following inventory methods results in the highest cost of goods sold?

(A) FIFO
(B) LIFO
(C) Average cost
(D) Periodic inventory
(E) Perpetual inventory

(A) (B) (C) (D) (E)

16. A company forecasts that during the next year it will be able to sell 80,000 units of its special product at a competitive selling price of \$10 per unit. The company has the capacity to produce 120,000 units per year. Its total fixed costs are \$528,000. Its variable costs are estimated at \$3 per unit. The company has the opportunity to sell 10,000 additional units during the same year at a special contract price of \$50,000. This special contract will not affect the regular sales volume or price. Acceptance of the contract will cause the year's net income to
- (A) increase by \$20,000
 - (B) increase by \$26,000
 - (C) increase by \$50,000
 - (D) decrease by \$50,000
 - (E) decrease by \$24,000
- (A) (B) (C) (D) (E)
17. Which of the following standard cost variances provides information about the extent to which the manufacturing plant of a company was used at normal capacity?
- (A) Materials quantity (usage) variance
 - (B) Labor efficiency (time) variance
 - (C) Labor rate variance
 - (D) Overhead spending (controllable) variance
 - (E) Overhead volume variance
- (A) (B) (C) (D) (E)
18. Equity investors are most interested in which aspect(s) of a company?
- I. Book value
 - II. Profitability
 - III. Cash flow
- (A) I only
 - (B) II only
 - (C) III only
 - (D) I and II only
 - (E) II and III only
- (A) (B) (C) (D) (E)

19. X Corporation declares and issues a 5 percent stock dividend on common stock, payable in common stock, shortly after the close of the year. All of the following statements about the nature and effect of the dividend are true EXCEPT
- (A) The total stockholders' equity in the corporation is not changed.
 - (B) The dividend does not constitute income to the stockholders.
 - (C) The book value per share of common stock is not changed.
 - (D) The amount of retained earnings is reduced.
 - (E) The amount of total assets is not changed.
- (A) (B) (C) (D) (E)
20. The financial statement that includes classifications for operating, financing, and investing activities of a business entity for a period of time is called the
- (A) Income Statement
 - (B) Statement of Retained Earnings
 - (C) Balance Sheet
 - (D) Statement of Changes in Owners' Equity
 - (E) Statement of Cash Flows
- (A) (B) (C) (D) (E)
21. A feature of the process cost system that is NOT a feature of the job order cost system is
- (A) computation of the equivalent units of production
 - (B) compilation of the costs of each batch or job produced
 - (C) use of the Raw Materials Inventory account
 - (D) preparation of a Cost of Goods Manufactured Statement for each accounting period
 - (E) application of manufacturing overhead on a predetermined basis
- (A) (B) (C) (D) (E)

22. Net purchases for the year amounted to \$80,000. The merchandise inventory at the beginning of the year was \$19,000. On sales of \$120,000, a 30 percent gross profit on the selling price was realized. The inventory at the end of the year was
- (A) \$13,000
 - (B) \$15,000
 - (C) \$17,000
 - (D) \$25,000
 - (E) \$63,000
- (A) (B) (C) (D) (E)
23. The balance sheet of Harold Company shows current assets of \$200,000 and current liabilities of \$100,000. The company uses cash to acquire merchandise inventory. As a result of this transaction, which of the following is true of working capital and the current ratio?
- (A) Both are unchanged.
 - (B) Working capital is unchanged; the current ratio increases.
 - (C) Both decrease.
 - (D) Working capital decreases; the current ratio increases.
 - (E) Working capital decreases; the current ratio is unchanged.
- (A) (B) (C) (D) (E)
24. "In determining net income from business operations, the costs involved in generating revenue should be charged against that revenue."
- The statement above best describes which of the following?
- (A) The cost principle
 - (B) The going-concern principle
 - (C) The profit principle
 - (D) The matching principle
 - (E) The business entity principle
- (A) (B) (C) (D) (E)

25. A long-term investment in stock classified as an available-for-sale security requires an end of the year adjustment that impacts on which of the following?
- (A) current assets
 - (B) stockholders' equity
 - (C) net income
 - (D) cash flow
 - (E) intangible assets
- Ⓐ Ⓑ Ⓒ Ⓓ Ⓔ

Study Resources

To prepare for the “Principles of Accounting” exam you should study the contents of at least one textbook designed for a full-year undergraduate course in principles of accounting. You can find textbooks used for college level accounting courses in many college bookstores. While most textbooks cover both financial and managerial accounting topics, their approach and emphasis varies. You may therefore wish to consult more than one textbook on the more important topics. When selecting a textbook, check the table of contents against the “Knowledge and Skills Required” section on pages 1-3.

Additional suggestions for preparing for CLEP exams are given in Chapter 1.

Answers to Sample Questions

Principles of Accounting

1. D
2. E
3. E
4. A
5. E
6. B
7. A
8. C
9. E
10. C
11. D
12. D
13. C
14. E
15. B
16. A
17. E
18. E
19. C
20. E
21. A
22. B
23. A
24. D
25. B